

## Message Text

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FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC IMMEDIATE 4160

C O N F I D E N T I A L SECTION 1 OF 4 BRASILIA 1681

NODIS

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3.O.11652: GDS

TAGS: OVIP (KISSINGER, HENRY A.)

SUBJECT: FINANCE MINISTER SIMONSEN'S PROPOSAL TO NEGOTIATE BILATERAL  
SOLUTION TO EXPORT SUBSIDY - COUNTERVAILING  
DUTY PROBLEM - EMBASSY'S COMMENTS

1. SUMMARY&7.33TING WITH FINANCE MINISTER SIMONSEN AND  
OTHER ECONOMIC MINISTERS HAS PROVIDED FIRST SBLIUD INDICATION  
THAT GOB MAY BE WILLING TO CONSIDER SUBSTANTIAL  
REVISIONS IN ITS SUBSIDY AND FISCAL SYSTEMS TO AVOID  
CONTINUING CONFLICT WITH THE US OVER COUNTERVAILING  
DUTY ISSUE. SIMONSEN, IN ESSENCE, OFFERED TO NEGOTIATE/  
A BILATERAL SOLUTION TO THIS PROBLEM WITHOUT AWAITING  
RESULTS OF MTN. WHILE SIMONSEN'S SPECIFIC PROPOSALS  
MAY BE EITHER NOT FEASIBLE OR MAY PRESENT CONSIDERABLE  
DIFFICULTIES, AT LEAST IN THEIR PRESENT FORM, WE BELIEVE  
THAT THEY PROVIDE AN IMPORTANT OPENING. WE RECOMMEND  
THAT, TAKING ADVANTAGE OF THE MOMENTUM CREATED BY THE  
SECRETARY'S VISIT, US PROMPTLY AGREE TO TRY TO  
NEGOTIATE A BILATERAL UNDERSTANDING. AT STAKE,  
ASIDE FROM LONG TERM FOREIGN POLICY CONSIDERATIONS,  
ARE IMPORTANT US ECONOMIC INTERESTS:  
BRAZILIAN OFFICIALS HAVE NOW MADE IT CLEAR THAT THEY  
WILL RESORT TO DIRECT ADMINISTRATIVE MEASURES  
TO DIVERT BRAZILIAN IMPORTS AWAY FROM THE US IF  
TRADE ISSUES CANNOT BE RESOLVED AND THE BILATERAL  
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TRADE DEFICIT IS NOT DIMINISHED. WE BELIEVE

MINISTER REISE VILLOSO'S VISIT TO WASHINGTON  
NEXT WEEK, THE FORTHCOMING MEETING OF THE BILATERAL  
SUB-GROUP ON TRADE, AND SECRETARY SIMON'S  
VISIT HERE WILL PROVIDE EXCELLENT OPPORTUNITIES  
TO PURSUE THESE NEGOTIATIONS. END SUMMARY.

2. IN OUR VIEW, THE SECRETARY'S MEETING WITH  
FINANCE MINISTER SIMONSEN AND PLANNING MINISTER  
REISE VELLOSO COULD TURN OUT TO BE AN IMPORTANT  
STEP IN THE DEVELOPMENT OF EASIER US-BRAZILIAN  
TRADE RELATIONS. SIMONSEN SHOWED GREATER-THAN-  
EXPECTED FLEXIBILITY BY INDICATING A WILLINGNESS  
TO MAKE SUBSTANTIAL REVISIONS IN BRAZIL'S  
EXPORT SUBSIDY-FISCAL INCENTIVE SYSTEM AND THUS  
TO NEGOTIATE A BILATERAL SOLUTION TO THE SUBSIDY-  
COUNTERVAILING DUTY PROBLEM. AT THE SAME TIME,  
REISE VELLOSO MADE CLEAR THAT THE GOB DOES NOT  
CONSIDER ITSELF ENTIRELY WITHOUT MEANS TO RETALIATE  
IF A BILATERAL SOLUTION TO THIS AND OTHER TRADE PROBLEMS  
CANNOT BE FOUND. SINCE THE GOB DIRECTLY CONTROLS  
ROUGHLY ONE HALF OF BRAZIL'S TOTAL IMPORTS -- THE  
PUBLIC SECTOR'S SHARE IN BRAZIL'S TOTAL IMPORTS --  
THE GOB CAN, IF THIS WERE DEEMED NECESSARY, EMPLOY  
ADMINISTRATIVE DIRECTIVES TO DIVERT IMPORTS AWAY FROM  
THE US. REISE VELLOSO AND SIMONSEN -- IN THE PRESENCE  
OF OTHER GOB SENIOR ECONOMIC OFFICIALS EXCEPT CENTRAL  
BANK PRESIDENT PAULO LIRA WHO WAS ABSENT FROM THE  
CITY -- STRESSED THAT BRAZIL WOULD CONSIDER THIS A  
NEGATIVE APPROACH AND WOULD NOT REALLY WISH TO FOLLOW  
IT. BRAZIL, THEY AFFIRMED, WAS SEEKING COOPERATIVE  
SOLUTIONS. SINCE THE GOB BELIEVE IN MULTILATERAL  
TRADE IT SOUGHT A NARROWING OF THE BILATERAL TRADE  
DEFICIT WITH THE US TO A MORE REASONABLE LEVEL,  
NOT ITS FULL ELIMINATION.

I. SIMONSEN'S PRESENTATION TO THE SECRETARY.

3. THE ESSENCE OF SIMONSEN'S PRESENTATION ON THE  
SUBSIDY - COUNTERVAILING DUTY PROBLEM CAN BE GROUPED  
UNDER TWO BROAD HEADINGS -- THE PREMISES OF HIS  
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APPROACH AND SPECIFIC PROPOSALS.

A. PREMISES.

4. TWO BASIC ASSUMPTIONS UNDERLIE HIS  
APPROACH.

(A) IN VIEW OF THE HUGE BILATERAL TRADE DEFICIT,

US IMPORT RESTRICTIONS ARE SEVERELY RESENTED. AS REGARDS THE COUNTERVAILING DUTY PROBLEM, THE UNCERTAINTY OF POSSIBLE US ACTION IS A MORE SERIOUS PROBLEM FOR THE GOB THAN THE COUNTERVAILING DUTY RATES THEMSELVES. UNCERTAINTY NOT ONLY IS A SERIOUS IRRITANT, BUT ALSO A SUBSTANTIAL IMPEDIMENT TO THE GOB'S EFFORT TO REDUCE THE TRADE IMBALANCE BY A STRATEGY OF EXPORT EXPANSION AND DIVERSIFICATION.

(B) THE GOB IS NOT PREPARED TO SOLVE THE PROBLEM BY SUBSTITUTING FOR THE EXPORT SUBSIDIES AN OPEN DEVALUATION. SIMONSEN IS FEARFUL OF THE INFLATIONARY PRESSURES SUCH AN OPEN DEVALUATION WOULD ENTAIL, AND THE REPERCUSSIONS ON THE FINANCIAL STRUCTURE OF BRAZIL'S BUSINESS SECTOR, GIVEN THE MAGNITUDE OF BRAZIL'S FOREIGN DEBT. HE BELIEVES THAT MASSIVE FINANCIAL RESCUE OPERATIONS WOULD BE REQUIRED TO ASSIST FIRMS IN DIFFICULTY, AND, MORE IMPORTANTLY, IS CONCERNED THAT SUCH AN EXPERIENCE WOULD DISCOURAGE AND DAMPEN FUTURE FOREIGN BORROWING.

B. PROPOSALS.

SIMONSEN OFFERED A GENERAL COMMENT AND THEN SET FORTH TWO SPECIFIC ALTERNATIVE PROPOSALS FOR SOLVING THE COUNTERVAILING DUTY PROBLEM.

(A) FUNDAMENTAL REFORM OF BRAZIL'S FISCAL INCENTIVE EXPORT SUBSIDY SYSTEM: WHILE TOUCHING ON THIS ONLY BRIEFLY, SIMONSEN SAID THAT MODIFICATION OR REMOVAL OF THE SYSTEM COULD BE ACCOMPLISHED, BUT WOULD TAKE UP TO THREE YEARS. HE DID NOT PURSUE THIS APPROACH.

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(B) DEFINITION OF OBJECTIONABLE SUBSIDIES (ALTERNATIVE -): ONE WAY OUT OF THE IMPASSE CREATED BY THE SUBSIDY-COUNTERVAILING DUTY PROBLEM COULD BE A BILATERAL AGREEMENT DEFINING WHAT CONSTITUTES AN OBJECTIONABLE SUBSIDY. BRAZIL WOULD THEN REPLACE SUCH PRACTICES BY OTHER INCENTIVES NOT CONSIDERED A BOUNTY OR GRANT UNDER US LAW.

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(C) DISGUISED DEVALUATION (ALTERNATIVE 2):  
ALTERNATIVELY, IF THE FIRST ALTERNATIVE WERE NOT  
FEASIBLE, BRAZIL WOULD BE WILLING TO CONSIDER THE  
EFFECTIVE ELIMINATION OF THE SUBSIDY SYSTEM  
WITHOUT A FORMAL DEVALUATION. TO ACCOMPLISH THIS,  
THE PRESENT SUBSIDIES WOULD BE REPLACED BY A UNIFORM  
BENEFIT TO ALL EXPORTERS EQUIVALENT TO THE HIGHER  
CRUZEIRO REVENUES OBTAINABLE UNDER A CRUZEIRO  
DEVALUATION BY A GIVEN PERCENTAGE. IMPORTERS  
WOULD SIMULTANEOUSLY BE SUBJECT TO A CORRESPONDING  
FINANCIAL BURDEN (AS THEY ARE NOW). THUS  
THE INCREASE IN THE CRUZEIRO COST OF IMPORTS  
WOULD BE PRECISELY THE SAME AS THAT RESULTING  
FROM AN OPEN DEVALUATION BY THE PERCENTAGE IMPLICIT  
IN THE EXPORT INCENTIVE SCHEME. UNDER SIMONSEN'S  
PROPOSAL, THE SECRETARY OF THE TREASURY WOULD  
RECOGNIZE THAT THE TWO SETS OF LINKED, UNIFORM  
IMPORT AND EXPORT MEASURES WERE EQUIVALENT TO A  
DEVALUATION OF THE CRUZEIRO AND INTENDED TO SUBSTITUTE  
FOR IT. ON THIS BASIS HE COULD MAKE A FINDING THAT  
THE EXPORT INCENTIVES DO NOT CONSTITUTE A BOUNTY OR  
GRANT WITHIN THE MEANING OF THE US LAW.

II. EMBASSY'S COMMENTS ON THE TWO SPECIFIC PROPOSALS.

5. ALTERNATIVE A: DEFINITION OF OBJECTIONABLE  
SUBSIDIES. IN OUR VIEW, THIS APPROACH DOES NOT  
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OFFER GREAT PROMISE IN THE FORM PRESENTED. IF,

HOWEVER, THERE IS FLEXIBILITY AT ALL IN THE BRAZILIAN POSITION, IT OFFERS INTERESTING POSSIBILITIES FOR A INTERIM AGREEMENT. WITH RESPECT TO SIMONSEN'S PROPOSAL AS PRESENTED, IT IGNORES THAT THE ELIMINATION OF EXPORT SUBSIDY PRACTICES IS A MAJOR US OBJECTIVE IN THE MULTILATERAL TRADE NEGOTIATION. WE DO NOT BELIEVE THAT THE US COULD ACCEPT, FOR AN INDEFINITE PERIOD, THE EXISTENCE OF SUBSTANTIAL EXPORT SUBSIDIES IN A MAJOR COUNTRY LIKE BRAZIL WITHOUT SERIOUSLY UNDERMINING ITS NEGOTIATING STRATEGY IN GENEVA. CRITICISM FROM US INDUSTRY WOULD BE SEVERE WERE THE ADMINISTRATION TO PROCEED IN THIS MANNER.

6. ON THE OTHER HAND, THERE EXISTS THE POSSIBILITY-- ASSUMING SOME BRAZILIAN FLEXIBILITY -- THAT WITH CERTAIN MODIFICATIONS THE PROPOSAL MIGHT SERVE AS THE BASIS OF AN INTERIM SOLUTION PENDING THE COMPLETION OF THE NEGOTIATIONS OF A MULTILATERAL CODE. US NEGOTIATIONS WOULD SEEK A REDUCTION IN THE BENEFITS TO BRAZILIAN EXPORTERS AND EARLY ELIMINATION OF THE MORE OBJECTIONABLE FORMS OF SUBSIDY UNDER A SPECIFIC AND RAPID PHASE-OUT SCHEDULE. IN THE MEANTIME, BY ACCELERATING THE MINI-DEVALUATIONS BRAZIL WOULD REDUCE THE NEED FOR THESE SUBSIDIES. THE TRADE ACT SPECIFICALLY GIVES THE SECRETARY OF THE TREASURY THE AUTHORITY TO NEGOTIATE SUCH INTERIM AGREEMENTS UNDER SECTION 303 (D).

7. ALTERNATIVE B: DISGUISED DEVALUATION. IF THE POLITICAL WILL EXISTS WITHIN THE U.S., THIS PROPOSAL --ALTHOUGH DIFFICULT FOR THE U.S. TO ACCEPT AND ALMOST CERTAIN TO INVITE CONSIDERABLE DOMESTIC CRITICISM --SEEMS TO US IN PRINCIPLE FEASIBLE AND WORTH EXPLORING IN THE PROPOSED NEGOTIATIONS. THE RELEVANT CONSIDERATIONS ARE:

(A) BASIC TO SIMONSEN'S PROPOSAL IS THE ASSUMPTION THAT THE SECRETARY OF THE TREASURY HAS THE FLEXIBILITY TO BASE HIS DETERMINATION OF WHAT IS A SUBSIDY PRINCIPALLY ON THE ECONOMIC EFFECTS OF

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THE PARTICULAR EXPORT INCENTIVE WITHIN THE TOTALITY OF BRAZILIAN EXPORT AND IMPORT MEASURES. IN THIS CONNECTION, WE NOTE THAT THE TRADE ACT DOES NOT DEFINE A BOUNTY OR GRANT. ADMINISTRATIVELY DETERMINED--ALTHOUGH NOW SUBJECT TO COURT REVIEW--THE DEFINITION OF WHAT CONSTITUTES A BOUNTY RELIES HEAVILY ON THE ECONOMIC EFFECTS OF A PARTICULAR MEASURE. THIS IMPORTANCE OF ECONOMIC CONSIDERATIONS IS WELL ESTABLISHED BY CURRENT ADMINISTRATIVE

PRACTICE; FOR EXAMPLE, COUNTERVAILING DUTY RATES ARE SET ON THE BASIS OF THE ACTUAL BENEFIT TO THE EXPORTER, NOT THE NOMINAL RATE OR MAXIMAL THEORETICAL BENEFIT. THUS, WE ASSUME THERE SHOULD BE NO BASIS LEGAL AND CONCEPTUAL OBSTACLES THAT WOULD RULE OUT A DISCUSSION OF THE MERITS OF SIMONSEN'S APPROACH.

(B) THE PROPOSAL APPEARS TO ENVISAGE UNIFORM BENEFITS FOR ALL EXPORTERS. ALTHOUGH SIMONSEN DID NOT EXPLICITLY COMMIT HIMSELF TO THIS UNIFORMITY OF BENEFIT, IT WOULD SEEM TO FOLLOW FROM THE BASIC RATIONALE OF THIS APPROACH. THUS, UNDER THIS PROPOSAL BRAZIL WOULD ELIMINATE ALL DISCRIMINATORY PREFERENTIAL TREATMENT OF SPECIFIC EXPORTS AND EXPORT SECTORS. SPECIAL BENEFITS TO EXPORTERS IN COMPARISON WITH THE EQUIVALENT BURDEN TO IMPORTERS WOULD ALSO BE ELIMINATED, I.E., A SPECIFIC CEILING WOULD BE ESTABLISHED FOR EXPORT INCENTIVES IN RELATION TO THE IMPORT MEASURES. IN HIS PRESENTATION SIMONSEN EXPLICITLY RECOGNIZED THIS LINKAGE AS FUNDAMENTAL TO THE ACCEPTABILITY OF HIS PROPOSAL TO THE SECRETARY OF THE TREASURY.

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(C) THE SPECIFIC MECHANISM WHICH SIMONSEN PROPOSED FOR THE IMPLEMENTATION OF THE NEW SYSTEM WOULD BE EXPORT CREDITS AT FAVORABLE RATES, NOT

SUBJECT TO MONETARY CORRECTION. SIMONSEN NOTED THAT WHILE HE UNDERSTOOD THE US DESIRE TO LIMIT SUCH FINANCING AND BRING IT UNDER INTERNATIONAL RULES, IN FACT SUCH FINANCING WAS A GENERALLY USED AND WIDELY ACCEPTED METHOD OF EXPORT PROMOTION. HE OBSERVED THAT THE UNITED STATES ITSELF, THROUGH THE EXPORT IMPORT BANK MECHANISM, CCC CREDITS, ETC., WAS USING THIS METHOD OF SUBSIDIZING ITS EXPORTS. THE NEW EXPORT FINANCING MECHANISM WOULD HAVE ITS COUNTERPART IN THE EXISTING IMPORT DEPOSIT REQUIREMENT (360 DAY DEPOSIT WITHOUT INTEREST, WITH NO MONETARY CORRECTION OF THE PRINCIPAL REFUNDED AT THE END OF THE PERIOD). WHILE SIMONSEN DID NOT SAY SO, WE SEE NO REASONS WHY THE SPECIFICS OF THIS CONCEPTUAL ALTERNATIVE, INCLUDING THE MAGNITUDE OF THE INCENTIVES AND THEIR MODE OF EXECUTION, SHOULD NOT BE NEGOTIABLE IF THE US WERE WILLING, IN PRINCIPLE, TO DISCUSS THE MERITS OF THE PROPOSAL.

III. THE EXCHANGE RATE ISSUE.

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8. WHILE WE ARE COGNIZANT OF THE NUMEROUS PROBLEMS RAISED BY BOTH ALTERNATIVES A AND B, THE CENTRAL ISSUE, IT SEEMS TO US, IS REALLY THE US ATTITUDE TOWARDS SIMONSEN'S EXCHANGE RATE POLICY. IN HIS PRESENTATION SIMONSEN, IN ESSENCE, CONCEDED THAT THE CRUZEIRO IS SUBSTANTIALLY OVERVALUED BUT ALSO SAID THAT BRAZIL WOULD NOT RESORT TO OPEN DEVALUATION. THERE IS INCREASING EVIDENCE THAT BRAZIL'S MOST DYNAMIC EXPORT SECTORS SUCH AS SOYBEANS HAVE DIFFICULTY RECOVERING COSTS AT THE CURRENT EXCHANGE RATE, WITH THE RESULT THAT SIMONSEN AND OTHERS FIND THEMSELVES WITH AN EVER LENGTHENING LIST OF PETITIONERS FOR NEW OR BIGGER EXPORT SUBSIDIES. THE EMBASSY'S OWN VIEW IS THAT A SIGNIFICANT ONE OR TWO STEP DEVALUATION WOULD PROBABLY BE DESIRABLE SINCE (A) IT CONFORMS TO BASIS US PHILOSOPHY OF LETTING MARKET FORCES COME INTO PLAY; (B) IT WOULD REDUCE INTERNAL PRESSURES ON THE GOB TO INCREASE SUBSIDIES; AND (C) REDUCTION AND ELIMINATION OF THE SUBSIDIES WOULD CONSIDERABLY REDUCE BILATERAL TRADE ISSUES BETWEEN BRAZIL AND THE US (ALTHOUGH, OF COURSE, ESCAPE CLAUSE ACTIONS, WHILE NOT SPECIFICALLY DIRECTED AT BRAZIL, WOULD CONTINUE TO BE AN IMPORTANT PROBLEM).

9. CONVERSELY, WE SHOULD BE SENSITIVE TO THE POTENTIAL POLITICAL COST OF APPEARING TO PRESSURE THE GOB TO CONSIDER A MAJOR DEVALUATION. BY ALL REPORTS, THERE HAS BEEN CONSIDERABLE DEBATE WITHIN THE ECONOMIC MINISTRIES ON THE MERITS OF A SUBSTANTIAL OPEN DEVALUATION, AND MANY, IF NOT MOST, ACADEMIC ECONOMISTS SEEM TO FAVOR IT. ON THE OTHER HAND, SIMONSEN HIMSELF, SUPPORTED IN THIS BY PAULO LIRA, APPEARS TO HAVE BEEN RESISTING THIS APPROACH. WE HAVE SEEN NO EVIDENCE THAT THERE IS MAJOR DISAGREEMENT FROM HIS POSITION AT THE MOST SENIOR LEVELS OF THE GOVERNMENT, AND BELIEVE THAT HIS POLICY HAS PRESIDENT GEISEL'S FULL SUPPORT.

IV. CONCLUSIONS.  
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10. IN SUMMARY, OUR CONCLUSIONS, LIMITED HERE TO THOSE DIRECTLY RELEVANT TO ECONOMIC CONSIDERATIONS, ARE AS FOLLOWS:

(A) A SERIOUS TRADE CONFLICT THROUGH A SUCCESSION OF COUNTERVAILING DUTY CASES ENTAILS A RISK TO NEAR AND LONGER TERM US COMMERCIAL INTERESTS IN BRAZIL. IT WOULD ACCELERATE THE RELATIVE DECLINE OF THE US TRADE AND INVESTMENT POSITION IN FAVOR OF THE EUROPEAN COMMUNITY AND JAPAN.

(B) THE EMBASSY, THEREFORE, ENDORSES SIMONSEN'S INITIATIVE LOOKING TOWARD THE NEGOTIATION OF SOME BILATERAL UNDERSTANDING ON THE SUBSIDY QUESTION PENDING THE COMPLETION OF THE NEGOTIATION OF A MULTILATERAL CODE IN GENEVA. WE BELIEVE THE NEGOTIATIONS WOULD HAVE A FAIR CHANCE OF SUCCESS ONCE THE TWO SIDES BEGIN TO ADDRESS THE PROBLEM SYSTEMATICALLY AND COMPREHENSIVELY. WE WOULD ASSUME THE PARTICULAR PROPOSALS ENCOMPASSED WITHIN SIMONSEN'S INITIATIVE ARE NOT DEFINITIVE AND FINAL POSITIONS BUT THAT MODIFICATIONS CAN BE OBTAINED IN THE COURSE OF THE NEGOTIATIONS. THE CONCERN AT THE VERY HIGHEST LEVELS OF THE BRAZILIAN GOVERNMENT OVER THE BILATERAL TRADE PROBLEMS, THE BASICALLY CONCILIATORY TONE OF SIMONSEN'S PRESENTATION AND THE SPECIFICITY OF HIS SUGGESTIONS PERSUADE US THAT SIMONSEN AND REIS FELLOSO ARE SERIOUS IN THEIR DESIRE TO FIND A SOLUTION AND THAT THEY ARE PREPARED TO CONSIDER PROGRESSIVE CHANGES IN THE BRAZILIAN SYSTEM IF GIVEN A BASIS BY THE US TO PROCEED. SILVEIRA AND THE FOREIGN MINISTRY MAY PRESENT OBSTACLES.



(C) THE PROBLEM OF FINDING A SOLUTION TO THE EXPORT SUBSIDY SYSTEM IS, IN A BASIC SENSE, CLOSELY LINKED TO THE PROBLEM OF BRAZIL'S OVERVALUED EXCHANGE RATE. SIMONSEN'S ABILITY TO REDUCE SUBSTANTIALLY THE EXPORT BENEFITS, WITHOUT DISASTROUS LOSSES IN EXPORTS, WILL ULTIMATELY DEPEND ON A CORRECTION OF THE, AT LEAST AT THIS TIME, SIGNIFICANTLY OVERVALUED RATE. AN INTERIM AGREEMENT INCORPORATING MODIFICATIONS  
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IN ALTERNATIVE A, WITH A PROGRESSIVE PHASE-DOWN OF THE BENEFITS, WOULD GIVE BRAZIL THE ADVANTAGE OF SOLVING THIS PROBLEM GRADUALLY, WITHIN THE SYSTEM OF MINI-DEVALUATIONS, WITH THE POSSIBILITY THAT THE OVERVALUATION MAY BE REDUCED BY A RECOVERY OF BRAZIL'S TERMS OF TRADE. AN AGREEMENT ALONG THE LINES OF SIMONSEN'S SECOND ALTERNATIVE (ALTERNATIVE B), ON THE OTHER HAND, DOES NOT DIRECTLY RAISE THE PROBLEM OF AN OPEN DEVALUATION SINCE IT ACCEPTS THE SUBSTITUTE OF A DISGUISED DEVALUATION. BOTH OF SIMONENS'S PROPOSALS, IT SEEMS TO US, OFFER INTERESTING STARTING POINTS FOR A NEGOTIATION, EVEN THOUGH THE FIRST APPROACH WOULD NOT APPEAR TO BE ACCEPTABLE, EVEN IN PRINCIPLE, IN ITS PRESENT FORM.

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(D) A POSSIBLE FORUM FOR SUCH NEGOTIATIONS, AT LEAST IN THE INITIAL PHASE, WOULD BE THE FORTHCOMING MEETING OF THE SUB-GROUP ON TRADE. WE UNDERSTAND THAT THE MINISTRY OF FINANCE EXPECTS TO HAVE STRONG REPRESENTATION ON THE BRAZILIAN DELEGATION. IF NECESSARY, WASHINGTON MAY WISH TO SET UP A SPECIAL INTERDEPARTMENTAL WORKING PARTY TO HANDLE THIS PROBLEM WITHIN THE SUB-GROUP. EVEN BEFORE THAT MEETING, REIS VELLOSO'S VISIT TO WASHINGTON NEXT WEEK WILL BE AN OPPORTUNITY TO EXPLORE FURTHER POSSIBLE APPROACHES AND CONCEPTS. THE EMBASSY BELIEVES THAT THE NEGOTIATIONS SHOULD BE PURSUED ENERGETICALLY SO THAT IF POSSIBLE A BILATERAL UNDERSTANDING, OR AT LEAST A DEFINITION OF ALL THE MAJOR ELEMENTS, COULD BE READY BY EARLY MAY. SECRETARY SIMON AND MINISTER SIMONSEN COULD THEN RESOLVE THE REMAINING ISSUES PERSONALLY AND, IF POSSIBLE, WOULD REACH FINAL UNDERSTANDING DURING THE SECRETARY'S VISIT.

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